Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
	)	
Telecommunications Relay Services and	)	CG Docket No. 03-123
Speech-to-Speech Services for	)	
Individuals with Hearing and Speech Disabilities	)	

REPORT AND ORDER AND DECLARATORY RULING

Adopted: October 26, 2007 **Released: November 9, 2007**

By the Commission: Commissioners Copps and Adelstein issuing separate statements.

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I. INTRODUCTION

1. In July 2006, the Commission released a Further Notice of Proposed Rulemaking[1] seeking comment on issues concerning the compensation of telecommunications relay services (TRS) providers from the Interstate TRS Fund (Fund).[2] In this *Report and Order and Declaratory Ruling* (*Order*) we: (1) adopt a new cost recovery methodology for interstate traditional TRS[3] and interstate Speech-to-Speech (STS)[4] based on the "MARS" plan ("Multi-state Average Rate Structure"), proposed by one of the providers[5]; (2) adopt a new cost recovery methodology for interstate captioned telephone

[1] *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CG Docket No. 03-123, Further Notice of Proposed Rulemaking, 21 FCC Rcd 8379 (July 20, 2006) (*2006 TRS Cost Recovery FNPRM*).

[2] TRS, created by Title IV of the Americans with Disabilities Act of 1990 (ADA), enables a person with a hearing or speech disability to access the nation's telephone system to communicate with voice telephone users through a relay provider and a communications assistant (CA). *See* 47 U.S.C. § 225(a)(3) (defining TRS); 47 C.F.R. § 64.601(14). As noted below, there are various forms of TRS. The Fund compensates providers of eligible interstate TRS services, and other TRS services not compensated by the states, for their reasonable costs of providing service. *See generally Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CC Docket Nos. 90-571 & 98-67, CG Docket No. 03-123, Report and Order, Order on Reconsideration, and Further Notice of Proposed Rulemaking, 19 FCC Rcd 12475, 12479-83, paras. 3-8 (June 30, 2004) (*2004 TRS Report & Order*).

[3] Traditional TRS is a text-based form of TRS with the text provided via a text telephone (TTY) and the Public Switched Telephone Network (PSTN). *See* 47 C.F.R. § 64.601(14). This service includes Spanish-to-Spanish relay. *See Telecommunications Relay Services for Individuals with Hearing and Speech Disabilities*, CC Docket No. 98-67, Report and Order and Further Notice of Proposed Rulemaking, 15 FCC Rcd 5140, 5154-55, paras. 28-31 (March 6, 2000) (*2000 TRS Order*) (mandating interstate Spanish-to-Spanish traditional TRS).

[4] STS is a form of TRS that allows persons with speech disabilities to communicate with voice telephone users through the use of specially trained CAs who understand the speech patterns of persons with disabilities and can repeat the words spoken by that person. *See* 47 C.F.R. § 64.601(12). STS is a mandatory service, so that all common carriers obligated to provide TRS and all states with a certified state TRS program must offer this service. *2000 TRS Order*, 15 FCC Rcd at 5149, para. 15.

[5] Hamilton Relay, Inc. (Hamilton) raised this proposal, which would base the compensation rate paid by the Fund on the average of the *intrastate* TRS rates paid by the states, in its petition for reconsideration of the *2004 TRS Report & Order*. Hamilton Relay Service, Inc., Petition for Reconsideration (filed Oct. 1, 2004) (*Hamilton Petition*).

(continued...)

service (CTS)[6] and interstate and intrastate Internet Protocol (IP) captioned telephone service (IP CTS)[7] based on the MARS plan; (3) adopt a cost recovery methodology for Internet Protocol (IP) Relay[8] based on price caps; (4) adopt a cost recovery methodology for Video Relay Service (VRS)[9] that adopts tiered rates based on call volume; (5) clarify the nature and extent that certain categories of costs are compensable from the Fund; and (6) address certain issues concerning the management and oversight of the Fund, including financial incentives offered to consumers to make relay calls and the role of the Interstate TRS Fund Advisory Council.

2. In addition, we adopt new compensation rates for these services as follows:

- For interstate <u>traditional TRS</u>, we adopt the MARS plan rate of <u>$1.592</u> per-minute based on the states' competitively bid compensation rates for intrastate traditional TRS and STS. This rate shall be effective for the remainder of the 2007-2008 Fund year on the first day of the month following the effective date of this *Order*.[10]
- For interstate <u>STS</u>, we adopt a rate of <u>$2.723</u> per-minute. This rate is based on the MARS plan rate of $1.592, but includes an additional $1.131 per minute in compensation that shall be directed for outreach, as set forth below. This rate shall be effective for the remainder of

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Hamilton also raised this issue in its application for review of the *2004 Bureau TRS Rate Order*, which adopted the compensation rates for the various forms of TRS for the 2004-2005 Fund year. *See Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CC Docket No. 98-67, Order, 19 FCC Rcd 12224 (June 30, 2004) (*2004 Bureau TRS Rate Order*), modified by *Telecommunications Relay Services and Speech-to Speech Services for Individuals with Hearing and Speech Disabilities*, CC Docket No. 98-67, Order, 19 FCC Rcd 24981 (Dec. 30, 2004) (*Modified 2004 Bureau TRS Order*).

[6] CTS is a form of TRS generally used by someone who can speak and has some residual hearing. A special telephone displays the text of what the other party is saying, so that the user can simultaneously both listen to what is said over the telephone (to the extent possible) and read captions of what the other person is saying. *See Telecommunications Relay Services, and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CC Docket No. 98-67, Declaratory Ruling, 18 FCC Rcd 16121 (Aug. 1, 2003) (*2003 Captioned Telephone Declaratory Ruling*). CTS is not a mandatory form of TRS, although that issue is subject to a pending petition. *See Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities; Internet-based Captioned Telephone Service*, CG Docket No. 03-123, Declaratory Ruling, 22 FCC Rcd 379, at 379-80, para. 1 n.3 (Jan. 11, 2007) (*2007 IP CTS Declaratory Ruling*).

[7] IP CTS is a form of captioned telephone service where the connection carrying the captions between the relay provider and the user is via the Internet, rather than the PSTN. *See generally 2007 IP CTS Declaratory Ruling*. IP CTS is not a mandatory form of TRS, and, pursuant to the *2007 IP CTS Declaratory Ruling*, is compensated at the IP Relay rate. *Id.*, 22 FCC Rcd at 390, para. 26.

[8] IP Relay is a text-based form of TRS that uses the Internet, rather than the PSTN, for the link of the call between the relay user and the CA. *See Provision of Improved Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CC Docket No. 98-67, Declaratory Ruling and Second Further Notice of Proposed Rulemaking, 17 FCC Rcd 7779 (April 22, 2002) (*IP Relay Declaratory Ruling*). IP Relay is not a mandatory form of TRS. *See 2004 TRS Report & Order*, 19 FCC Rcd at 12564, paras. 231-32 (raising issue whether IP Relay should be a mandatory service).

[9] VRS is a form of TRS that that enables the VRS user and the CA to communicate via a video link in sign language, rather than through text. VRS presently requires a broadband Internet connection. *See 2000 TRS Order*, 15 FCC Rcd at 5152-54, paras. 21-27 (recognizing VRS as a form of TRS); 47 C.F.R. § 64.601(17) (defining VRS). VRS is not a mandatory form of TRS. *See 2004 TRS Report & Order*, 19 FCC Rcd at 12567-68, paras. 243-45 (raising issue whether VRS should be a mandatory service).

[10] The effective date of this Order with respect to the 2007-2008 rates adopted pursuant to the new cost recovery methodologies is 30 days after publication in the Federal Register. *See infra* para. 111.

the 2007-2008 Fund year on the first day of the month following the effective date of this *Order*.

- For interstate CTS and interstate and intrastate IP CTS, we adopt the MARS plan rate of $1.629 per-minute based on the states' competitively bid compensation rates for intrastate captioned telephone service. This rate shall be effective for the remainder of the 2007-2008 Fund year on the first day of the month following the effective date of this *Order*.
- For interstate and intrastate IP Relay, we adopt the rate of $1.293. This rate shall be effective for the 2007-2008 through 2009-2010 Fund years, subject to annual adjustment as set forth below.
- For interstate and intrastate VRS, we adopt the following rates and tiers: (1) for the first 50,000 monthly minutes: $6.77; (2) for monthly minutes between 50,001 and 500,000: $6.50; and (3) for monthly minutes above 500,000: $6.30. The VRS rates shall be effective for the 2007-2008 through 2009-2010 Fund years, subject to annual adjustment as set forth below.[11]

II. BACKGROUND

A. The Provision and Compensation of TRS

3. The *2006 TRS Cost Recovery FNPRM* and prior orders have set forth in detail the evolution of TRS and the compensation of providers from the Fund for the various forms of TRS, and therefore we do not repeat that history here.[12] We note, however, that Congress mandated that TRS users cannot be required to pay for the service costs of using TRS. Specifically, Congress provided that TRS users cannot be required to pay rates "greater than the rates paid for functionally equivalent voice communication services with respect to such factors as the duration of the call, the time of day, and the distance from point of origination to point of termination."[13] Therefore, the cost of relay facilities, and

[11] On June 29, 2007, the Consumer & Governmental Affairs Bureau (CGB) released the 2007-2008 TRS rate order, extending the 2006-2007 per-minute rates but adopting a new Fund size and carrier contribution factor. *See Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CG Docket No. 03-123, Order, 22 FCC Rcd 11706 (June 29, 2007) (*2007 Bureau TRS Rate Order*). Although we are adopting new rates for certain services, we do not in this *Order* amend the Fund size or carrier contribution factor. If necessary, we will make an appropriate adjustment later in the Fund year to account for these revised rates, or do so in conjunction with the revised carrier billing that will be necessary as a result of the recent order requiring interconnected VoIP providers to contribute to the Fund. *See IP-Enabled Services*, WC Docket No. 04-36, *Implementation of Sections 255 and 251(a)(2) of The Communications Act of 1934, as Enacted by The Telecommunications Act of 1996: Access to Telecommunications Service, Telecommunications Equipment and Customer Premises Equipment by Persons with Disabilities*, WT Docket No. 96-198, *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CG Docket No. 03-123, *The Use of N11 Codes and Other Abbreviated Dialing Arrangements*, CC Docket No. 92-105, Report and Order, 22 FCC Rcd 11275 (June 15, 2007) (*Sections 225/255 VoIP Order*).

[12] *See 2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8381-84, paras. 2-6. Recent TRS compensation rate orders include: *2007 Bureau TRS Rate Order*; *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CG Docket No. 03-123, Order, 21 FCC Rcd 7018 (June 29, 2006) (*2006 Bureau TRS Rate Order*); *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CG Docket No. 03-123, Order, 20 FCC Rcd 12237 (June 28, 2005) (*2005 TRS Rate Order*); *2004 Bureau TRS Rate Order*; *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities*, CC Docket No. 98-67, Order, 18 FCC Rcd 12823 (June 30, 2003) (*2003 Bureau TRS Rate Order*).

[13] *See* 47 U.S.C. § 225(d)(1)(D); 47 C.F.R. § 64.604(c)(4).

the relaying of the calls, cannot be passed on to consumers of TRS, since doing so would result in TRS users paying rates greater than those for similar voice telephone calls.

4. As a result, Section 225 creates a cost recovery regime whereby providers of TRS are compensated for their costs of providing TRS.[14] Section 225 provides that the "costs caused by" interstate TRS "shall be recovered from all subscribers for every interstate service," and the "costs caused by" the provision of intrastate TRS "shall be recovered from the intrastate jurisdiction."[15] With respect to interstate TRS, contributions are collected from the common carriers providing interstate telecommunications services to create the Fund from which eligible TRS providers may be compensated.[16]

5. Under the present interstate cost recovery methodology, providers are compensated on the basis of a per-minute compensation rate.[17] This rate is not a "price" that is charged to, and paid by, a service user, but rather is a settlement mechanism to ensure that providers are compensated from the Fund for their reasonable actual costs of providing service. Presently, compensation rates are determined annually based on the providers' projected cost and minutes of use data for a two-year period.[18] This data is submitted to the Fund administrator, presently the National Exchange Carrier Association (NECA), which then calculates the average per-minute compensation rate for the various forms of TRS and submits

[14] 47 U.S.C. § 225(d)(3).

[15] 47 U.S.C. § 225(d)(3)(B); *see also* 47 C.F.R. § 64.604(c)(5)(ii). No specific funding method is required for intrastate TRS or state TRS programs. States generally recover the costs of intrastate TRS either through rate adjustments or surcharges assessed on all intrastate end users, and reimburse TRS providers directly for their intrastate TRS costs. Most states presently select one provider to offer TRS within the state. On an interim basis, the costs of providing intrastate VRS, IP Relay, and IP CTS are presently compensated from the Interstate TRS Fund. *See 2000 TRS Order*, 15 FCC Rcd at 5154, para. 26 (addressing VRS); *IP Relay Declaratory Ruling*, 17 FCC Rcd at 7786, para. 20 (addressing IP Relay); *IP CTS Declaratory Ruling*, 18 FCC Rcd at 16125, para. 10 (addressing IP CTS). The issue of separation of costs relating to the provision of IP Relay and VRS is pending pursuant to the *FNPRM* in the *2004 TRS Report & Order*. *See 2004 TRS Report & Order*, 19 FCC Rcd at 12561-65, paras. 221-30 (IP Relay), 12565-67, paras. 234-42 (VRS).

[16] The amount of each carrier's contribution is the product of the carrier's interstate end-user telecommunications revenue and a contribution factor determined annually by the Commission. 47 C.F.R. § 64.604(c)(5)(iii). As noted above, interconnected VoIP providers are now also required to contribute to the Fund. *See supra* note 11; *Sections 225/255 VoIP Order*.

[17] Compensation is presently based on per-minute rates adopted each year by the Commission for the following July 1 to June 30 Fund year. There are currently four different compensation rates for the different forms of TRS: traditional TRS, IP Relay, STS, and VRS. *See 2006 Bureau TRS Rate Order*, 21 FCC Rcd at 7024-25, paras. 17-18 (adopting separate rates for traditional TRS and IP Relay). The traditional TRS rate applies to Spanish Relay service and captioned telephone service. Presently, the IP Relay rate applies to IP CTS. *See 2007 IP CTS Declaratory Ruling*, 22 FCC Rcd at 390, para. 26.

[18] *See* 47 C.F.R. § 64.604(c)(5)(iii)(C).

the rates to the Commission for approval.[19] The Commission (or Bureau)[20] issues a rate order each year by June 30, either approving or modifying these rates.[21]

6. During the first 10 years of the TRS program, the calculation and adoption of the interstate TRS compensation rates was largely uneventful, in large part because, until 2000, there was only one compensation rate – the rate for traditional TRS. That has not been the case, however, in more recent years, particularly with respect to VRS. As a result of the *2000 TRS Order,* in 2000, the first VRS compensation rate was adopted, $5.143.[22] The rate subsequently rose to $17.04 per-minute,[23] and as a result the number of providers offering this service increased. In more recent years, the Commission disallowed some of the providers' submitted costs (in particular, profits or mark-ups on expenses) and the VRS rate has been in the six or seven dollar per-minute range.[24]

7. As a result of the increased use of VRS and its relatively high compensation rate (compared to those for the other forms of TRS), the Fund has grown from approximately $40 million in 2000 to over $550 million for the 2007-2008 Fund year. Over $430 million of this $550 million, or nearly 75 percent, is attributable to VRS.[25] As we have noted, carriers offering interstate telecommunications services contribute to the Fund, and these costs are generally passed on to their consumers.

B. The *2006 TRS Cost Recovery FNPRM*

8. Because the annual determination of the TRS compensation rates has presented a variety of regulatory and administrative challenges under the present methodology, in the *2006 TRS Cost Recovery FNPRM*, the Commission sought comment on a range of issues concerning the compensation of

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[19] *See, e.g.,* NECA, *Interstate Telecommunications Relay Services Fund Payment Formula and Fund Size Estimate,* CG Docket No. 03-123, filed May 1, 2007 (*2007 NECA Filing*). The regulations provide that the Fund administrator shall administer the Interstate TRS Fund and oversee both the collection of contributions paid into the Fund and the compensation of TRS providers from the Fund. *See* 47 C.F.R. § 64.604(c)(5)(iii).

[20] Some rate orders have been at the Commission level, and some have been at the Bureau level. *See supra* note 12 (citing orders).

[21] *Id.*; *see, e.g., 2006 Bureau TRS Rate Order* (most recent order adopting annual per-minute compensation rates based on providers' projected costs and minutes of use); *2003 Bureau TRS Rate Order*, 18 FCC Rcd at 12836, para. 37 (disallowing certain costs and adopting a modified rate).

[22] *See generally 2003 Bureau TRS Rate Order*, 18 FCC Rcd at 12830, para. 18 n.52 (setting forth history of VRS compensation rates).

[23] *Id.*; *see also* www.neca.org (Resources, then TRS) (chart of the history of all TRS compensation rates).

[24] *Id.*; *2004 Bureau TRS Order*, 19 FCC Rcd at 12237-41 paras. 35-46 (addressing cost disallowances and challenges to the adoption of the 2004-2005 compensation rates); *2005 TRS Rate Order*, 20 FCC Rcd at 12246-48, paras. 23-28 (adopting 2005-2006 VRS rate based on median rate of the providers because record reflected that the average rate would unfairly penalize most providers and providers' cost projections may have been based on various levels of service quality); *2006 Bureau TRS Rate Order*, 21 FCC Rcd at 7027, paras 28-29 (freezing the 2005-2006 VRS rate for the 2006-2007 Fund year because, in part, of the providers' difficulty in accurately predicting minutes of use); *2007 Bureau TRS Rate Order* (extending the 2006-2007 rates); 2004 *TRS Report & Order,* 19 FCC Rcd at 12537-52, paras. 163-200 (addressing challenges to the 2003-2004 compensation rates, including disallowances for profit, engineering costs, and labor costs); *2006 Order on Reconsideration* (addressing challenge to 2003-2004 VRS role); *Telecommunications Relay Services and Speech-to-Speech Services for Individuals with Hearing and Speech Disabilities,* CG Docket No. 03-123, *Memorandum Opinion and Order*, 21 FCC Rcd 8063 (July 12, 2006) (*2006 MO&O*) (addressing challenge to 2004-2005 TRS rates).

[25] *2007 Bureau TRS Rate Order*, 22 FCC Rcd at 11714, para 27; *2007 NECA Filing* at 21 (estimating 65 million minutes of use for VRS for the 2007-2008 Fund year).

relay providers from the Fund.[26] More particularly, the Commission sought comment on four issues: (1) the adoption of an alternative cost recovery methodology for traditional TRS, STS, and IP Relay based, in some fashion, on Hamilton's MARS plan[27]; (2) the adoption of an alternative cost recovery methodology for VRS; (3) whether certain types of costs are appropriately compensable from the Fund, and if so, the nature and extent of such costs; and (4) the management and administration of the Fund, including ways to combat waste, fraud, and abuse.

1. Cost Recovery Methodology for Traditional TRS, STS, and IP Relay

9. The Commission first sought comment on adoption of the MARS plan for determining the compensation rate for traditional TRS, as well as for STS and IP Relay.[28] As the Commission explained, under the MARS plan, the interstate traditional TRS rate would be calculated based on a weighted average of the *intrastate* TRS rates paid by the states.[29] The Commission sought comment on whether the MARS plan, because it is based on competitively bid state rates, would provide for a more efficient provision of service and result in a fairer, more reasonable compensation rate. The Commission

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[26] We note that some comments filed in response to NECA's 2006 and 2007 filings of proposed compensation rates for the 2006-2007 Fund year by providers reflect dissatisfaction with the rate setting process, as well as with the proposed rates. *See* NECA, *Interstate Telecommunications Relay Services Fund Payment Formula and Fund Size Estimate,* CG Docket No. 03-123, filed May 1, 2006 (*2006 NECA Filing*); *2007 NECA Filing*; Sprint Nextel Corporation (Sprint Nextel) Comments (May 17, 2006) at 1-2; Communication Services for the Deaf, Inc. (CSD) Comments (May 17, 2006) at 6-8; Hamilton Comments (May 17, 2006) at 8-9; Hands On Video Relay Services, Inc. (Hands On) Reply Comments (May 24, 2006) at 17; CSD Reply Comments (May 24, 2006); *see also* Telecommunications for the Deaf, Inc., National Association of the Deaf, Deaf and Hard of Hearing Consumer Advocacy Network, and California Coalition of Agencies Serving the Deaf and Hard of Hearing (collectively, Consumer Groups) Reply Comments (May 24, 2006); TRS Advisory Council *Ex Parte* comments (July 21, 2006). Further, *ex parte* letters were filed by KPS Consulting on behalf of Ultratec (May 9, 2007); Ruth Milkman on behalf of Sorenson (May 11, 2007); Francis Buono on behalf of Sprint Nextel, Sorenson, and Snap!VRS (May 11, 2007); KPS Consulting on behalf of Ultratec (May 16, 2007); Ruth Milkman on behalf of Sorenson, Sprint Nextel, and Snap! VRS (May 23, 2007); Toni R. Acton on behalf of AT&T (May 23, 2007); Bob Segalman and Rebecca Ladew (May 24, 2007); Ruth Milkman on behalf of Sprint Nextel, Sorenson, and Snap!VRS (May 31, 2007); Ruth Milkman on behalf of Sprint Nextel, Sorenson, and Snap!VRS (June 1, 2007); Ruth Milkman on behalf of Sprint Nextel, Sorenson, and Snap!VRS (June 1, 2007); George L. Lyon, Jr. on behalf of HOVRS (June 5, 2007); KPS Consulting on behalf of Ultratec (June 6, 2007); (KPS Consulting on behalf of CSDVRS, HOVRS, GoAmerica, and CACDHH-VRS (June 12, 2007); Eliot J. Greenwald on behalf of TDI (June 15, 2007); David A. O'Conner on behalf of Hamilton (June 15, 2007); David A. O'Conner on behalf of Hamilton (June 15, 2007); Ruth Milkman on behalf of Sprint Nextel, Sorenson, and Snap!VRS (June 15, 2007); KPS Consulting on behalf of CSDVRS (June 16, 2007); Eliot J. Greenwald on behalf of TDI (June 20, 2007); Aileen A. Pisciotta on behalf of Speech Communication Assistance by Telephone, Inc. (SCT) (June 22, 2007); George Lyon, Jr. on behalf of HOVRS (June 26, 2007); Michael B. Fingerhut filed by Ruth Milkman on behalf of Sprint Nextel, Snap, and Sorenson (June 27, 2007) (corrected version); George Lyon, Jr. on behalf of HOVRS (July 5, 2007); George Lyon, Jr. *Ex Parte* on behalf of HOVRS (July 11, 2007); Bob Segalman (July 17, 2007); KPS Consulting on behalf of CSDVRS (July 19, 2007); David A. O'Conner on behalf of Hamilton (August 10, 2007); Ruth Milkman on behalf of Sprint Nextel, Snap, and Sorenson (August 10, 2007).

[27] The Commission noted that the compensation rate for traditional TRS applied to captioned telephone service. *2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8387, para. 17 & n.59. Therefore, the *2006 TRS Cost Recovery FNPRM* did not expressly address the cost recovery methodology for captioned telephone service. *But see id.*, 21 FCC Rcd at 8386, para. 13 (seeking comment on whether the MARS plan should apply to traditional TRS "and possibly other forms of TRS, such as STS"). Further, at this time, IP CTS had not yet been recognized as a form of TRS.

[28] *Id.*, 21 FCC Rcd at 8385-88, paras. 9-19.

[29] *Id.*, 21 FCC Rcd at 8385, para. 9. In contrast, the present methodology is based on projected cost and demand data submitted by the providers.

also sought comment on various details of how the MARS plan might be implemented, including reconciling state compensation rates based on session minutes rather than conversation minutes,[30] whether any factors might warrant excluding a particular state's rate from the calculation,[31] and whether the individual state rates should be weighted by a state's total minutes of use, so that states with relatively high rates and low minutes of use do not skew the average.[32]

10. The Commission also sought comment on the application of the MARS plan to STS.[33] Because many states compensate intrastate traditional TRS and intrastate STS at the same rate,[34] and NECA recommended that the Commission consider adopting one rate that would apply to both STS and traditional TRS,[35] the Commission sought comment on whether the same rate should apply to both traditional TRS and STS.[36] Finally, the Commission sought comment on whether the traditional TRS, STS, and IP Relay rate(s) should continue to be set for a one-year period or whether a longer rate period might be appropriate.[37]

2. Cost Recovery Methodology for VRS

11. Although the Commission has sought comment several times on the appropriate VRS cost recovery methodology,[38] it concluded that because of the continued sharp growth in the use of VRS,

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[30] *Id.*, 21 FCC Rcd at 8387, para. 14. As the Commission noted, presently the Fund compensates providers for conversation minutes (or completed minutes), which are measured by conversation time between the calling and called party. Conversation minutes do not include time for call set-up, ringing, waiting for the called party to answer, or call wrap-up, and do not encompass calls that reach a busy signal or are not answered. Session minutes include all the time the CA spends on a call to the relay center, *i.e.*, from the time the call is connected to the CA, regardless of whether the called party answers the call. *Id.*, 21 FCC Rcd at 8385, para. 9 n.41.

[31] For example, if a state rate is based on the interstate rate, inclusion of that state's rate into the MARS plan would be circular. *See id.*, 21 FCC Rcd at 8387, para. 15.

[32] *Id.*, 21 FCC Rcd at 8387, para. 16.

[33] *Id.*, 21 FCC Rcd at 8387-88, para. 17 (also noting that STS is a mandatory form of TRS and states compensate providers for intrastate STS calls). The compensation rate for traditional TRS presently also applies to Spanish relay and captioned telephone service.

[34] *See generally 2006 NECA TRS Rate Filing* at 17.

[35] *Id.*

[36] *2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8388, para. 18.

[37] *Id.*, 21 FCC Rcd at 8389, para. 23.

[38] *Id.*, 21 FCC Rcd at 8389-90, para. 24; *see generally 2000 TRS Order*, 15 FCC Rcd at 5152-56, paras. 22, 26-27, 32-33 (directing the TRS Advisory Council to develop cost recovery guidelines for VRS; the Council recommended using the same methodology for VRS as used for traditional TRS); *Telecommunications Services for Individuals with Hearing and Speech Disabilities, Recommended TRS Cost Recovery Guidelines, Request by Hamilton Telephone Company for Clarification and Temporary Waivers*, CC Docket No. 98-67, Memorandum Opinion and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 22948, 22958-60, paras. 30-36 (Dec. 21, 2001) (declining to adopt a permanent cost recovery methodology for VRS and seeking additional comment on this issue); *2004 TRS Report & Order*, 19 FCC Rcd at 12487-90, paras. 17-24 (declining to adopt a permanent cost recovery methodology for VRS), at 12565-67, paras. 234-40 (*FNPRM* seeking additional comments and noting that although the Commission had previously sought comment on this issue, the relative infancy and unique characteristics of VRS made it difficult to determine what the appropriate cost recovery methodology should be). In response to the *2004 TRS Report and Order's FNPRM*, six VRS providers filed comments. CSD Comments (Oct. 18, 2004); Hamilton Comments (Oct. 18, 2004); Hands On Comments (Oct. 15, 2004); MCI Comments (Oct. 18, 2004); Sorenson Comments (Oct. 18, 2004); Sprint Comments (Oct. 18, 2004). Four providers supported the use of the compensation methodology currently in use for VRS and all other forms of TRS. Commenters generally opposed

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open issues concerning what costs may appropriately be included in determining the compensation rate under the current methodology, and the providers' difficulty in accurately forecasting demand,[39] it was appropriate to seek additional comment on this issue.[40] The Commission emphasized that it was particularly interested in adopting a methodology that would result in more predictability for the providers, and be consistent with the principle that providers are entitled to their "reasonable" actual costs of providing service.[41] The Commission therefore sought comment on whether modifications should be made to the current methodology, or whether a new methodology should be adopted. The Commission proposed various new methodologies, including compensating each provider based on the provider's actual, reasonable costs, seeking competitive bids,[42] or using a true-up based on each provider's reasonable actual costs.

12. With respect to use of a true-up, the Commission sought comment on whether providers should be required to reimburse the Fund for any amount by which their payments exceed reasonable actual costs.[43] The Commission also sought comment on whether "the VRS compensation rate should be set for a two-year period, rather than a one-year period."[44]

3. "Reasonable" Costs Compensable from the Fund

13. The Commission noted that NECA's Data Collection Form sets forth categories of costs related to the provision of TRS for which providers may seek compensation.[45] The Commission sought comment on the nature and extent to which certain types of costs may be compensated from the Fund

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NECA's method of reviewing the providers' projected cost and demand data, including the disallowance of certain expenses. *See generally 2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8390-91, para. 26.

[39] Based on its review of the providers' filings for the 2006-2007 Fund year, the Commission expressed concern that the providers' data reflected virtually no growth in the projected use of VRS in 2006 and 2007. *See 2006 Bureau TRS Rate Order*, 21 FCC Rcd at 7022, para. 11 (citing *2006 NECA Filing* at Ex. 1D). In fact, the use of VRS has continued to rapidly rise in the 2006-2007 Fund year: from 3.2 million minutes in January, to 3.6 million minutes in July, to over 4.2 million minutes in December, and to nearly 5.3 million minutes in May 2007. *See 2007 NECA Filing*; www.neca.org (Resources, then TRS) (monthly reports of minutes of use).

[40] *See 2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8391, para. 27. The Commission also noted that since 2004 the Commission has adopted VRS speed of answer and interoperability requirements, which may affect cost recovery issues. In addition, the Commission noted that it recently permitted entities desiring to offer VRS to be certified by the Commission, which it expected would result in new VRS providers offering service, many of which will not be traditional telephone companies and therefore may present unique cost issues. *Id.*

[41] *Id.*, 21 FCC Rcd at 8391, para. 28.

[42] *Id.*, 21 FCC Rcd at 8389-92, paras. 24-29. The Commission noted that many states award contracts for the provision of intrastate TRS to a single provider through a competitive bidding process, which, as noted above, is the basis for the MARS plan. *Id.*, 21 FCC Rcd at 8391, para. 28 n.82.

[43] The Commission noted that the providers' demand forecasts for VRS have generally been significantly lower than actual demand, and under the current cost recovery methodology, when demand is underestimated, the compensation rate will be higher, resulting in potential overcompensation for actual minutes. *Id.*, 21 FCC Rcd at 8392, para. 29. The Commission also noted that it previously sought comment in 2004 on whether the VRS cost recovery methodology should include a true-up. *Id.*, 21 FCC Rcd at 8392, para. 29 n.83 (seeking comment on whether VRS might be compensated by "a lump sum payment or periodic payments of estimated actual costs with a 'true-up' at the end of the fund year" (quoting *2004 TRS Report & Order*, 19 FCC Rcd at 12565-66, para. 236)).

[44] The Commission also sought comment on whether the VRS compensation rate should be set for a two-year or longer period, rather than a one-year period. *Id.*, 21 FCC Rcd at 8392, paras. 30.

[45] *See 2006 NECA Filing* at Appendix A.

consistent with Section 225, including marketing and outreach expenses,[46] overhead costs, legal and lobbying expenses, start-up expenses, and executive compensation.[47]

14. The Commission also sought comment on whether provider cost and demand data should be made public to make it easier for providers and the public to comment on the reasonableness of the rates.[48] The Commission noted that it has honored requests by providers submitting projected cost and demand data to treat that information as confidential and, as a result, the Commission addresses such data only in the aggregate or in some other way that does not reveal the individual data of a particular provider.[49] The Commission also recognized that this approach makes it is difficult for providers and the public (including carriers providing interstate telecommunications services that pay into the Fund) to comment on the reasonableness of the rates.[50] As a result, the Commission sought comment on whether the providers' projected (and/or actual) cost and demand data, or particular categories of the cost and demand data, should be made public, and on other ways to make the rate setting process more transparent.[51]

4. Management and Administration of the Fund

15. Finally, the Commission sought comment on the steps it might take to ensure the integrity of the Fund and that compensation is paid consistent with the statute. Specifically, the Commission sought comment on the oversight of the Fund administrator, the oversight of the providers, and ways to deter waste, fraud, and abuse.[52] The Commission emphasized that it sought to ensure that "with the number of providers and number of minutes of use continuing to increase, particularly with respect to VRS and IP Relay, the Fund compensates providers only for legitimate minutes of use provided in compliance with the mandatory minimum standards, and that the compensation rates are based on accurate demand and cost data."[53]

III. REPORT AND ORDER

A. TRS Cost Recovery Methodologies

1. The Cost Recovery Methodology for Interstate Traditional TRS, Interstate STS, Interstate CTS, and IP CTS – the MARS Plan

a. Adoption of the MARS Plan

16. As discussed more fully below, we adopt a cost recovery methodology for interstate traditional TRS, interstate STS, interstate CTS, and interstate and intrastate IP CTS based on the MARS plan – *i.e.*, a weighted average of competitively bid state rates. We believe that this approach will

[46] In the *2006 NECA Filing*, "marketing/advertising" was described as "[e]xpenses associated with promoting TRS services within the community." "Outreach" was described as "[e]xpenses of programs to educate the public on TRS." *See id.*

[47] *See 2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8393-97, paras. 33-42. The Data Collection Form explicitly includes some of these cost categories, and implicitly includes others. *See generally 2006 NECA Filing* at Appendix A.

[48] *2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd. at 8397, paras. 43-44.

[49] *Id.*, 21 FCC Rcd at 8397, para. 43 (citing *2004 Bureau TRS Order*, 19 FCC Rcd at 12232, para. 18 n.57); *see also* 47 C.F.R. § 64.604(c)(5)(iii)(I) (generally providing that Fund administrator shall keep all data confidential).

[50] *2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8397, para. 43.

[51] *Id.*, 21 FCC Rcd at 8397, para. 44.

[52] *Id.*, 21 FCC Rcd at 8398-99, paras. 45-49.

[53] *Id.*, 21 FCC Rcd at 8399, para. 49.

simplify the rate setting process and result in more predictable, fair, and reasonable rates. We will calculate one MARS rate applicable to both interstate traditional TRS and interstate STS based on state rates for intrastate TRS and STS (which are generally the same); we will adopt a separate MARS rate for interstate captioned telephone service and IP CTS based on state rates for intrastate captioned telephone service.

17. Presently, the compensation rates are based on a weighted average of the providers' *projected* minutes of use of the service, and their *projected* costs of providing these minutes, for a future two-year period.[54] This methodology has several inherent drawbacks. First, the resulting rate is only as accurate as the providers' projected minutes of use and costs. Providers have an inherent incentive to submit *higher,* rather than lower, costs to ensure the compensation rate is as high as possible to cover their costs and presumably make a profit.[55] For the same reason, they have an incentive to underestimate minutes of use.[56] We also recognize that, under the present cost recovery methodology, the resulting rates do not correlate precisely to any of the providers' actual costs.

18. We believe the MARS plan, because it is based on competitively bid state rates, produces a rate that better approximates providers' reasonable costs, and therefore promotes the efficient recovery of all costs. Further, the MARS plan eliminates the costs, burdens, and uncertainties associated with evaluating, correcting, and re-evaluating provider data.[57]

19. Most commenting providers support using the MARS plan as the cost recovery methodology for at least some forms of TRS.[58] Hamilton, the proponent of the plan, states that the MARS plan is easy to implement, offers regulatory certainty, and more closely approximates providers' reasonable costs than the current rate methodology or any other methodology suggested in the *2006 TRS Cost Recovery FNPRM*.[59] Hamilton further asserts that detailed cost calculations for categories such as marketing, outreach, legal costs, lobbying costs, executive compensation, and overhead costs would be unnecessary under the MARS plan, because the plan relies on competitively based state rates.[60] Hamilton explains that because the Commission certifies each state's TRS program, the individual state TRS

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[54] In other words, the determination of the rate for the July 1, 2007, to June 30, 2008, Fund year is based on the providers' projected minutes of use and costs for calendar years 2007 and 2008.

[55] This is true even though, when actually offering service, providers have an incentive to minimize their costs, since presently they are compensated at the weighted average national rate regardless of their actual costs and therefore, in effect, earn "profit" on the difference between their actual costs and the compensation rate.

[56] *See supra* note 39 (noting that the providers' filings for the 2006-2007 Fund year reflected virtually no growth in the projected minutes of use of VRS, but in fact VRS minutes have continued to grow rapidly).

[57] *See* Hamilton Comments at 6-7. In this regard, we will no longer require traditional TRS, STS, CTS, and IP CTS providers to file the annual cost and demand data reports with the Fund administrator, as they have in the past. They will, however, have to file data related to state traditional TRS and STS rates, as dicussed below.

[58] In addition to Hamilton, commenters supporting the MARS plan include Hands On, Verizon, AT&T, and Ultratec. *See, e.g.,* Hands On Comments at 4-9 (supporting MARS plan for traditional TRS, STS, and IP Relay, but not VRS); Verizon Comments at 7 (supporting MARS plan only for traditional TRS); AT&T Reply Comments at 2 (supporting MARS plan only for traditional TRS); Ultratec Reply Comments at 1-2 (supporting MARS plan for captioned telephone service).

[59] Hamilton Comments at 2. Verizon notes that "the relatively large number of competitors and the considerable number of bidding opportunities provide the Commission with a wealth of information about the appropriate competitive rates for providing traditional TRS in specific, competitive state markets." Verizon Comments at 3; *see also* Hamilton Reply Comments at 2 (noting Verizon's comments).

[60] Hamilton Comments at 7.

programs' costs are "presumptively reasonable" and should be deemed not to include extraneous costs.[61] Hamilton also notes that the MARS plan accounts for states with low TRS rates as well as those with high TRS rates, and that an average of those competitive rates will result in a reasonable, competitively-based interstate TRS rate.[62] Hamilton further asserts that the MARS plan can be used for traditional TRS, STS, IP Relay and possibly captioned telephone service.[63]

20. Verizon and AT&T support the MARS plan for traditional TRS, but not for STS, IP Relay, or VRS because there are no "market-based rates" for these services.[64] Verizon asserts that, for traditional TRS, setting an interstate rate based on a weighted average of intrastate rates will yield an "accurate, market-driven rate sufficient to cover provider costs while encouraging efficiency."[65] AT&T asserts that "[t]he competitive bidding process necessarily encourages providers to minimize costs and increase productivity."[66] Ultratec supports the MARS plan for captioned telephone service, but states that the rate should be based on state captioned telephone rates rather than state traditional TRS rates.[67]

21. We disagree with Sprint Nextel's opposition to the MARS plan for traditional TRS and STS.[68] Sprint Nextel asserts that the MARS plan would create new burdens and uncertainties, including developing and applying appropriate weighting factors and ensuring that call minutes are treated consistently.[69] As outlined below, we do not believe that this will be the case; in any event, particular facets of the MARS can be adjusted in future years if necessary. Sprint Nextel also argues that rates based on state rates – even competitively bid state rates – may not be based on efficient costs.[70] Although it is possible that some individual state rates may be relatively high because of inefficiencies or specific state requirements, we anticipate that the overall effect of any such rates on the final MARS rate will be minimal because of the large number of state rates (some relatively high, some relatively low) that will be averaged together.[71] Sprint Nextel further argues that there is no certainty that the MARS plan will lead

[61] Hamilton *Ex Parte* (Feb. 12, 2007) at 1.

[62] *Id.*

[63] *See generally* Hamilton Comments at 2-8; *see also* Hamilton Reply Comments at 4-9.

[64] *See* Verizon Comments at 1-8; *see also* AT&T Reply Comments at 3 (stating that it supports Verizon's approach, but also that it "could" support the MARS plan for IP Relay). Hamilton asserts, however, that the MARS rate can apply to IP Relay and STS because the costs are "virtually the same as traditional TRS." *See* Hamilton Reply Comments at 2.

[65] Verizon Comments at i.

[66] AT&T Reply Comments at 2.

[67] Ultratec Reply Comments at 2 (noting that "[t]he market-driven, competitively based rate that would come out of this process would be both reasonable and meet the telecommunications needs of consumers, because it will draw on the expertise and analyses of all the states providing [captioned telephone service]"); *see also* Hamilton Reply Comments at 7 (a separate MARS rate can be calculated for captioned telephone service because states generally contract separately for that service); Sprint Nextel Mar. 13, 2007 *Ex Parte* (although opposing the MARS plan, arguing that if it is adopted, a separate MARS rate for captioned telephone service should be adopted).

[68] *See* Sprint Nextel Comments at 7-8. *See generally* Sorenson Comments at 58-59 (opposing MARS plan for VRS and IP Relay because there is no state data for these services upon which to base a rate). CSD, the Joint Consumers, the Joint Providers, and the FL PSC do not address the MARS plan.

[69] Sprint Nextel Comments at 8; *see also* Sprint Nextel Mar. 13, 2007 *Ex Parte.*

[70] Sprint Nextel Comments at 8 (asserting, for example, that if a "state insists that the provider open a relay center in the state so as to create jobs for its citizens rather than allow the provider to handle the state's TRS traffic at a regional center located outside of the state," costs may be higher).

[71] *See* Verizon Comments at 5.

to lower rates.[72] Our mandate, however, is not to achieve any particular rate level, but to ensure that the rates correlate to actual reasonable costs and that the *process* of determining the rates is fair, efficient, and predictable.[73]

22. Sprint Nextel also asserts that the Commission does not have the authority to implement the MARS plan because it constitutes a delegation of the Commission's responsibilities under Section 225 to the states.[74] Sprint Nextel asserts that if the MARS plan is viewed as a delegation to the states of the Commission's responsibility under Section 225 to set interstate TRS compensation rates, "it would be beyond the Commission's authority to adopt," citing *USTA v. FCC*.[75] Hamilton disagrees, asserting that the adoption of the MARS plan would not be a delegation of authority to the states. Hamilton argues that under the MARS plan, "the Commission would gather information about competitively-bid rates at the state level. The Commission would then use that information to calculate the interstate TRS rate."[76]

23. We agree with Hamilton and do not believe that using the MARS plan to determine TRS compensation rates paid by the Fund delegates to the states the Commission's responsibility to set TRS rates. Under the MARS plan, the Commission simply gathers existing data from the states, and uses that data, along with other data, to determine the interstate compensation rate under its own rate methodology.[77] This action is therefore distinguishable from that in *USTA v. FCC* cited by Sprint Nextel, where the court found that the Commission delegated to an outside party (a state) a responsibility given the Commission by statute. When the Commission uses the MARS plan to determine TRS compensation rates, the Commission has retained, and is exercising, its responsibility to adopt TRS compensation rates.[78]

24. Finally, Sprint Nextel asserts that a "price-cap" plan should be implemented for all forms of TRS, while the Joint Providers assert that price-cap plan should be implemented for VRS and IP Relay.[79] Under this approach, a fixed compensation rate would apply for a specified period of time for each form of TRS compensated by the Fund. This rate would then be adjusted, "upward based on the Gross Domestic Product – Price Index ('GDP-PI') and downward by a productivity factor."[80] Sprint Nextel argues that this approach "eliminate[s] the discretion afforded NECA and the Commission to

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[72] Sprint Nextel Comments at 8. Hamilton states that the Commission's obligation is to ensure that providers are compensated for their reasonable costs, not to guarantee that relay rates are lowered over the long run. Hamilton Reply Comments at 3. Hamilton also asserts that if a provider's price submission is not based on efficient cost data, that provider likely will not be the successful bidder. *Id.* at 4.

[73] *See* Hamilton Reply Comments at 3-4.

[74] Sprint Nextel Comments at 7 n.7.

[75] *Id.* (citing *USTA v. FCC*, 359 F.3d 554 (D.C. Cir.), *cert. denied*, 125 S. Ct. 316 (2004)).

[76] Hamilton Reply Comments at 3.

[77] *See id.*; *see also infra* paras. 26-38, addressing the implementation of the MARS plan.

[78] Indeed, the court in *USTA v. FCC*, addressing the Commission's delegation to the states of the determination of which network elements shall be available to competitive local exchange companies on an unbundled basis, reasoned that when authority is delegated to an "outside" party, "lines of accountability may blur, undermining an important democratic check on government decision-making." *USTA v. FCC*, 359 F.3d at 565. Under the MARS plan, the Commission remains fully responsible for the adoption of the rates.

[79] *See* Joint Provider Comments at 3-13, Sprint Nextel Comments at 5-7. We also address price caps below. *See infra* paras. 42-43, 50-52.

[80] Sprint Nextel Comments at 6. Sprint asserts that "such a formula would assure that the cap would be reduced each year during the initial three year period." *Id.* at 7.

disallow costs reported by providers without conducting the necessary cost studies to determine whether such costs were reasonably incurred."[81]

25. For forms of TRS for which state rates are available, we believe the MARS plan is a better approach for determining the interstate compensation rate for the same service. As we have noted, under the TRS regime the compensation rate is not a "price" that is charged to, and paid by, a service user, but rather is a settlement mechanism to ensure that providers are compensated from the Fund for their actual reasonable costs of providing service. The MARS plan uses an average of competitively bid state rates as a measure of those reasonable costs. It also eliminates the need to review and possibly disallow costs reported by providers. Under price caps, we would have to determine an initial rate that accurately reflects providers' historical, actual, reasonable costs. The best measure of these costs, where available, is the compensation rates by states for the same, *albeit* intrastate, service.[82] Therefore, for those services for which there are competitively bid state rates, we believe the MARS plan is superior to price caps.

b. Calculation of the MARS Plan Rate for Interstate Traditional TRS and Interstate STS

26. We set forth below how the MARS plan rate for interstate traditional TRS and interstate STS will be calculated. First, the MARS plan rate will be calculated annually by the Fund administrator,[83] and filed with the Commission by May 1st of each year. Although we sought comment on whether the rate period should be longer than one year to create more predictability for the providers,[84] we will continue to adopt new rates on an annual basis, as under the MARS plan there should be less variation in the rates from year to year. If that proves not to be the case, we will revisit whether the rate should be set for a longer period of time. Second, the rate will be based on intrastate traditional TRS and STS data for each state for the prior calendar year. In addition, because some states compensate a much larger number of minutes than others, we will calculate a weighted average rate by dividing total state dollars paid by total conversation minutes. Further, in calculating total state dollars (the numerator), we will make adjustments that reflect that fact that some state rates are based on session minutes, and some state rates are based on conversation minutes. The calculations will also take into consideration the fact that some states may compensate intrastate traditional TRS and intrastate STS at different rates, and that for some states the contractual per-minute compensation rate does not include all of the costs paid by the state to the provider for the relay service.[85] Finally, we will monitor implementation of the MARS plan and, if necessary, take further steps to ensure that the MARS rate compensates providers for their reasonable costs of providing service.[86]

[81] *Id.* at 5-6. Sprint Nextel also argues that customers and carriers that pay into the Fund would benefit from the realized efficiencies of the price-caps through the application of a formula to determine prices for a three-year period. *Id.* at 5-7.

[82] *See infra* paras. 50-52 for a more extensive discussion of price cap proposals in the context of a VRS cost recovery methodology.

[83] For the Fund year that begins July 1, 2007, the MARS plan rate may be calculated by the Commission in conjunction with the Fund administrator upon the effective date of this *Order.*

[84] *See generally 2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8389, para. 23.

[85] *See* Sprint Nextel *Ex Parte* (March 13, 2007) (asserting that if the Commission adopts the MARS plan, the calculation should include "all of the rate elements paid by a state for TRS service, including any monthly recurring charges [MRCs] paid by a state to cover non-traffic sensitive rates incurred by the TRS provider").

[86] Sprint Nextel has also stated that if the MARS plan is adopted, it should provide for adjustment mid Fund year to reflect changes in state rates. *Ex Parte* letter filed by Francis M. Buono on behalf of Sprint Nextel, Sorenson, and

(continued...)

27. As described more fully below, the determination of the rate by the Fund administrator will include the following steps: (1) the collection of intrastate traditional TRS and STS compensation rate data from the states and the providers for the prior calendar year, and the determination of whether any state's data will be excluded from the calculation; (2) the calculation of each state's total dollars paid for intrastate traditional TRS and STS services during the applicable period; and (3) the calculation of the final rate by dividing the total dollars paid by all states by the total conversation minutes of all states.[87] The proposed MARS rate and a description of how it was calculated will be placed on public notice. By June 30th, the Commission will release an order adopting the compensation rate for the following July 1st to June 30th Fund year.

28. *Collection of State Data.* Each January,[88] the Fund administrator will request that each state TRS administrator file with the Commission the following information related to the provision and compensation of intrastate traditional TRS and STS in the state for the previous calendar year: (1) the per-minute compensation rate(s) for intrastate traditional TRS and STS; (2) whether the rate applies to session minutes or conversation minutes[89]; (3) the number of intrastate session minutes for traditional TRS[90] and STS; and (4) the number of intrastate conversation minutes for traditional TRS and STS.[91] If the contractual per-minute compensation rate does not include all of the costs paid by the state to the provider for the relay service, the state should also list other amounts paid to the provider during the relevant calendar year. Because some states that compensate intrastate minutes based on session time may not have data indicating the number of intrastate conversation minutes, the Fund administrator will also request that each provider of interstate traditional TRS and STS file with the Commission the same data noted above.[92] The Commission or Fund administrator will also ask each state and provider to indicate what information should be considered confidential; as discussed below, the specifics of such information will not be publicly released.[93]

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Snap!VRS (May 11, 2007). We decline to adopt this approach but, as noted, will monitor the MARS rate as well as changes to state rates to determine if such an adjustment procedure should be adopted in the future.

[87] We note that an allowance for working capital to the rate is unnecessary because, as Hamilton notes, "working capital is already built into the various state rates" that underlie the MARS rate. Hamilton *Ex Parte* (Feb. 12, 2007) at 1.

[88] We intend to use the January timeframe beginning in January 2008 with respect to the 2008-2009 Fund year (and the collection of calendar 2007 data). We have already collected the relevant data from the states and providers for the 2007-2008 Fund year.

[89] *See supra* note 30, addressing "session" and "conversation minutes." Conversation minutes are a subset of session minutes.

[90] References to traditional TRS include Spanish-to-Spanish traditional TRS.

[91] If a state compensates intrastate traditional TRS and STS at the same rate, total session and conversation for minutes for these services may be reported together. If STS is compensated at a different rate, the state should set forth the number of session and conversation minutes for traditional TRS and the number of session and conversation minutes for STS.

[92] *See* 47 C.F.R. § 64.604(c)(5)(iii)(C) (requiring providers to submit to the Fund administrator "true and adequate data necessary to determine TRS Fund revenue requirements and payments," including "total TRS minutes of use, total interstate TRS minutes, total TRS operating expenses, ... total TRS investment, ... and other historical or projected information reasonably requested by the administrator for purposes of computing payments and revenue requirements"); Hamilton *Ex Parte* (Feb. 12, 2007) at 2 (noting that the Commission can obtain this information from both the states and the providers).

[93] *See* Appendix B for sample template for this data to be obtained from the states.

29. We understand that some states enter into multi-year contracts for the provision of intrastate traditional TRS and/or STS that may or may not conform to calendar years.[94] Therefore, if the intrastate compensation rate(s) paid by a state for these services changed during the calendar year, or the provider changed, the state and the providers should list each rate separately and indicate the time period in which each rate was effective, whether the rate applied to session or conversation minutes, and the amount of conversation and session minutes associated with each period. In this way, each rate will be proportionally factored into the ultimate MARS rate. In addition, we recognize that some state's data may have to be excluded for the MARS rate calculation. For example, if a state's intrastate rate is based on the interstate rate, that rate will not be used in the MARS calculation.[95] Although there may be other reasons to exclude a particular state's data, which we will address on a case by case basis, we agree that we should not generally exclude a state's data simply because it may be based on additional requirements in the state contract. Our rules contemplate that state programs may include standards that exceed the TRS mandatory minimum standards, and require that in such cases the state show that its program is nevertheless consistent with Section 225 and the regulations.[96] Moreover, as noted above, averaging nearly 50 state rates will necessarily include some that are relatively low and some that are relatively high.[97]

30. *Calculating Total State Costs.* Using the above-listed data collected from the states and the providers, the Fund administrator will multiply each state's TRS rate by the number of either intrastate session minutes or intrastate conversation minutes, whichever the state rate is based upon.[98] The total dollar amount for each state will then be totaled. This number becomes the numerator in the final calculation that determines the rate.[99]

31. *Final Calculation of the Rate.* To determine the final MARS rate to be applied to interstate conversation minutes, the total dollar amount for all the states (including costs not reflected in the rate) is divided by the total intrastate traditional TRS and STS *conversation* minutes for all the states (even if some states do not base their rate on conversation minutes).[100] This proposed MARS rate, and a description of how it was calculated, will be placed on public notice. By June 30th, the Commission (or Bureau) will adopt the final compensation rate for the Fund year.

32. Under this approach, we do not need to calculate a conversation "factor" to conform session minutes to conversation minutes. Because we are calculating an interstate rate that will be applied to conversation minutes, for states that compensate conversation minutes we simply multiply the number

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[94] *See* Hamilton Comments at 6 ("Hamilton is aware of about seven states that change per-minute rates annually").

[95] *See id.* at 4; Hamilton Reply Comments at 2-3. Presently we are aware of only one state (California) that may fall into this category.

[96] *See* 47 C.F.R. § 64.605(b). We expect that the number of states whose data is excluded from the MARS calculation will be very small.

[97] *See* Hamilton *Ex Parte* (Feb. 12, 2007) at 1 (asserting that state TRS rates are presumptively reasonable, and that the "MARS plan is beneficial in that it accounts for states with low TRS rates as well as those with high TRS rates, and that an average of those competitive rates will result in a reasonable, competitively-based interstate TRS rate").

[98] In other words, if the state pays the provider based on session minutes, then the state rate is multiplied by session minutes; if the state pays the provider based on conversation minutes, then the state rate is multiplied by conversation minutes. As a practical matter, the TRS rates paid for session minutes are lower than that rates paid for conversation minutes because, for any particular call, the session minute time is greater than the conversation minute time. If the state has a separate rate for intrastate STS, the STS minutes will not be included with the traditional TRS minutes, but will separately be multiplied by the STS rate. *See* Appendix B.

[99] *See* Appendix C for sample calculation of this data.

[100] *See* Appendix D for sample calculation of the final rate.

of conversation minutes by the state rate, and include that amount in the numerator.[101] For states that compensate session minutes, however, because the session time for a relay call will be longer than the conversation time, rates paid for session minutes are generally lower than rates paid for conversation minutes. Therefore, to avoid artificially reducing the MARS rate, for such states the state rate is multiplied by the larger number of session minutes, and that total is included in the numerator.[102] In short, because each state's dollar amount that is reflected in the numerator (*i.e.*, total dollars of all states) is based on each state's compensation rate multiplied by either total session or conversation minutes, depending on the basis for the state rate, under this approach the resulting MARS rate takes into account the inherent difference between state rates based on session minutes and state rates based on conversation minutes.[103]

33. Similarly, the "weighting" of each state's rate in comparison to the other states' rates is built into the calculation. States with a larger number of minutes will constitute a proportionately larger amount of both the numerator (total state dollars paid) and the denominator (total conversation minutes) in calculating the MARS rate. Further, each state's practice with regard to the "rounding" of call minutes – *e.g.*, to the nearest second or to the nearest minute – is not relevant because we can reasonably assume that bidders will adjust their proposed compensation rate to the state's rounding practice.[104]

34. Finally, although historically we have calculated a separate compensation rate for interstate STS calls based on the providers' projected costs and minutes of use for that service,[105] as noted above we adopt a single MARS rate that will apply to both traditional TRS and STS based on the state intrastate rates and minutes of use for both services. Because the states generally compensate intrastate traditional TRS and STS calls at the same rate, and generally the same providers offer these services, we believe that, absent some unusual circumstances or specific needs of providers or consumers of one of the services, the Fund should be compensating interstate STS calls at the same rate.[106]

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[101] *See* Hamilton Reply Comments at 5-6; Hamilton *Ex Parte* (Feb. 12, 2007) at 2-3.

[102] *See* Hamilton Reply Comments at 5-6; Hamilton *Ex Parte* (Feb. 12, 2007) at 2-3.

[103] In its initial comments, Hamilton proposed using a conversation factor to conform state rates that are based on session minutes to rates based on conversation minutes. Hamilton Comments at 3-4. In its Reply Comments, however, Hamilton explained that this would not be necessary if "each state's total number of intrastate minutes is multiplied by that state's intrastate rate." Hamilton Reply Comments at 5-6; *see also* Hamilton *Ex Parte* (Feb. 12, 2007) at 2-3 (explaining that a conversion factor is unnecessary).

[104] For example, if the state rounds all calls to the nearest minute, a provider can expect to be compensated for a larger number of minutes, and therefore will adjust its bid accordingly. In other words, projected volume will affect the proposed rate.

[105] *See* www.neca.org (Resources, then TRS) (chart of the history of all TRS compensation rates). We note that average monthly interstate STS minutes have recently ranged between 14,000 and 17,000, compared to over one million for traditional TRS. *See* NECA *TRS Fund Performance Status Report, Funding Year July 2006 – June 2007*, available at www.neca.org (Resources, then TRS).

[106] Between 2001 and 2004, the compensation rate for STS was significantly higher than the traditional TRS compensation rate. *See 2006 Bureau TRS Rate Order*, 21 FCC Rcd at 7021, para. 7 n.32 ("[s]ince its inception, the compensation rate for STS has ranged from $1.596 to $4.263 per-minute"); *see also 2004 Bureau TRS Order*, 19 FCC Rcd at 12232-12233, para. 21 n.63 (history of STS compensation rates). More recently, the rates have become much closer. For the 2006-2007 Fund year, the STS rate was $1.409 and the traditional TRS rate was $1.291. *See also 2007 Bureau TRS Rate Order* (extending the 2006-2007 rates to the 2007-2008 Fund year). However, NECA reports that based on the providers' projected cost and demand data, with disallowances, the 2007-2008 STS rate would be $3.26 (compared to a similarly calculated traditional TRS rate of $1.69). *2007 NECA Filing* at 12, 18. Notwithstanding this recent data suggesting a greater disparity between the providers' traditional TRS and STS costs, we believe that, as a general matter, because states compensate these services at the same rate, use of the MARS plan requires that the same interstate rate apply to these services. *See generally* Hamilton Comments at 4

(continued…)

35. In sum, we believe that the MARS plan will simplify the determination of the annual compensation rate for interstate traditional TRS and interstate STS and result in a rate that reflects the reasonable costs of providing service based on the rates states pay through competitive bidding for the same, *albeit* intrastate, service.[107] In addition, for those services to which it applies, the MARS plan also avoids the necessity of detailed analysis (and possible disallowance) of the projected cost and demand data for each provider, as such data will no longer be required to be filed by the providers of these services.[108] To the extent future or unforeseen circumstances suggest that the MARS rate is not fair and reasonable, we can make adjustments as appropriate. Our objective is to ensure that services are provided efficiently and that providers are compensated for their reasonable actual costs of doing so. We believe that the MARS plan fulfills that goal.[109]

c. Calculation of the MARS Plan Rate for Interstate CTS and IP CTS

36. We also will use the MARS plan to calculate a separate compensation rate for interstate CTS and interstate and intrastate IP CTS. In the *2003 Captioned Telephone Declaratory Ruling,* the Commission concluded that interstate CTS calls would be compensated at the same rate as traditional TRS calls.[110] Hamilton asserts, however, that a separate compensation rate for CTS calls can be calculated under the MARS analysis because those states that have contracted for this service pay a separate rate.[111] Although Sprint Nextel generally opposes the MARS plan, it maintains that if the MARS plan is adopted, a separate MARS rate should be calculated for CTS.[112] Ultratec, which addresses only

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("Most states compensate traditional TRS and STS services at the same rate."); Hamilton *Ex Parte* (Feb. 12, 2007) at 3 (noting 18 state RFPs of which it is aware that apply the same rate to traditional TRS and IP Relay). Also, the Fund administrator and the Interstate TRS Advisory Council have supported compensating these services at the same rate. *See* 2006 NECA Filing at 17 & n.32; Hamilton *Ex Parte* (Feb. 12, 2007) at 3. As we have noted, the calculation of the MARS rate will take into consideration the fact that a particular state has separate rates for traditional TRS and STS. At the same time, in a particular Fund year unusual circumstances may require the Commission to make adjustments to the MARS rate of the one of these services.

[107] We recognize that the number of bidders for a particular state contract may affect the ultimate state rate, and that if there are only a few bidders for a contract the resulting state rate may be higher than it would be if there were more bidders. We believe that this issue will be self-correcting over time. In any event, we will revisit this issue in the future to determine whether there are a sufficient number of bidders for state TRS contracts to ensure that particular state rates are not artificially high and that application of the MARS plan to interstate services results in reasonable rates.

[108] *See supra* note 57.

[109] As noted above, states may request that their data be treated as confidential. At the same time, we recognize that there is a strong public interest in making the basis for the compensation rate as transparent as possible. For this reason, as Hamilton suggests, we will disclose the total intrastate conversation minutes and the total intrastate TRS dollars (the numerator and denominator in the MARS calculation, respectively) and the rate derived thereby. *See* Hamilton *Ex Parte* (Feb. 12, 2007) at 2. We will also disclose all of the state rates, and whether they are based on session or conversation minutes, in a random order and without identifying the particular states. In this way, the public will be advised of critical aspects of the rate calculation, but the confidentiality of individual state rates and minutes of use will be maintained. *See id.*

[110] *See 2003 Captioned Telephone Declaratory Ruling*, 18 FCC Rcd at 16128, para. 22.

[111] Hamilton Reply Comments at 7-8.

[112] Sprint Nextel Mar. 13, 2007 *Ex Parte*; *Ex Parte* filed by Francis Buono (May 11, 2007) at 3.

CTS, supports the MARS plan for this service, and asserts that the rate should be based on state CTS rates rather than state traditional TRS rates.[113]

37. We agree that because we are adopting the MARS plan for traditional TRS and STS, and there are separate state rates for intrastate CTS, a separate MARS rate should be calculated for this service. Accordingly, we will also request that state administrators and interstate CTS providers file with Commission the information set forth in paragraph 28 above as applied to the provision of intrastate CTS, as requested by the Fund administrator. The calculation of the CTS MARS rate will be consistent with the analysis set forth above and in the examples set forth in Appendices B, C, and D.

38. With respect to IP CTS, although the *2007 IP CTS Declaratory Ruling* concluded that IP CTS calls would be compensated at the same rate as IP Relay calls,[114] we now conclude that IP CTS should be compensated at the same rate as CTS.[115] IP CTS is a new service without cost history and, upon further examination, we believe that the cost recovery rate for CTS will more accurately reflect the reasonable actual costs of providing IP CTS. As a result, we will compensate IP CTS at the CTS MARS rate.[116]

2. The Cost Recovery Methodology for IP Relay

39. From its inception in 2002 through the 2004-2005 Fund year, IP Relay was compensated at the same rate as interstate traditional TRS.[117] In the *2005 TRS Rate Order,* the Commission, for the first time, adopted a separate rate for IP Relay.[118] The Commission explained that because the providers' cost and demand data indicated that IP Relay costs were approximately 11 percent less that traditional TRS costs, it was not appropriate to use the same rate for both services.[119] The Commission adopted a rate of $1.278 for IP Relay, and $1.440 for traditional TRS, for the 2005-2006 Fund year.[120] The following year, the Commission also adopted separate rates, but the difference in the rates was two-tenths of one cent ($1.291 for traditional TRS and $1.293 for IP Relay).[121]

40. Because all IP Relay calls are presently compensated from the Fund, there are no state IP Relay rates to which the MARS analysis can be applied directly. Hamilton asserts, however, that because the costs associated with providing IP Relay and traditional TRS are essentially the same, the traditional

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[113] Ultratec Reply Comments at 2 (noting that "[t]he market-driven, competitively based rate that would come out of this process would be both reasonable and meet the telecommunications needs of consumers, because it will draw on the expertise and analyses of all the states providing [captioned telephone service]").

[114] *See 2007 IP CTS Declaratory Ruling*, 22 FCC Rcd at 390, para. 26.

[115] *See generally* Comments of Ultratec, Inc. on NECA proposed Compensation Rates for July 2007 Through June 2008, CC Docket No. 03-123 (May 9, 2007) (asserting that IP CTS should not be compensated at the IP Relay rate).

[116] Because we are adopting the MARS plan for CTS and IP CTS, providers of these services will no longer be required to file annual cost and demand data submissions with the Fund administrator, although they will have to file other MARS-related data as requested by the Fund administrator. *See supra* note 57.

[117] *See 2004 Bureau TRS Rate Order,* 19 FCC Rcd at 12230-31, para. 17 n.54; *IP Relay Declaratory Ruling,* 17 FCC Rcd at 7786, para. 22 (noting that the record reflected that IP Relay and traditional TRS calls exhibited "very similar cost and demand characteristics").

[118] *2005 TRS Rate Order*, 20 FCC Rcd at 12243-45, paras. 16-20.

[119] *Id.*, 20 FCC Rcd at 12244, para. 20 (nothing that, as a result of the cost differential, if a combined rate was applied IP Relay providers would be overcompensated, and traditional TRS providers would be undercompensated).

[120] *See id.*, 20 FCC Rcd at 12237, para 1.

[121] *2006 Bureau TRS Rate Order*, 21 FCC Rcd at 7018-19, para. 1.

TRS MARS rate should also be applied to IP Relay.[122] Verizon does not support the MARS plan for IP Relay, because they argue, there are no "market-based rates" for that service.[123] AT&T, however, states that it could support the MARS plan for IP Relay because it uses the same CAs and equipment to provide IP Relay and traditional TRS, and therefore "its cost in providing these two services is not materially different.[124]

41. We conclude that the MARS methodology, as proposed, is not appropriate for IP Relay because there are no state rates for this service. Although we believe that the costs of providing traditional TRS and IP Relay are generally similar – in many instances, for example, the same CAs, sitting at the same offices, handle both traditional TRS and IP Relay calls – we are also concerned that that use of the MARS rate for IP Relay may result in the overcompensation of IP Relay providers.[125] As a result, we conclude that we will continue to calculate a separate compensation rate for IP Relay.

42. In their comments, the Joint Providers suggest implementing a price cap plan for regulating IP Relay rates.[126] The plan is based on the price cap plan implemented for incumbent LECs.[127] Under the plan, the compensation rate be set for a period of three years, "during which time the rates would be adjusted upward annually for inflation (according to a pre-defined inflation factor) and downward to account for efficiency gains (according to a factor also set at the outset of price caps).[128] The Joint Providers assert that this approach would have at least three benefits: (1) it would create incentives for providers to lower costs; (3) the three year time frame gives providers "predictability about revenue to allocate money to programs that will reduce costs in the future"; and (3) it simplifies the rate setting process, saving time and money.[129] Sprint Nextel also emphasizes that under price caps, providers would focus on increasing efficiencies to accommodate decreasing rates.[130]

43. We adopt a price cap plan for IP Relay based on the Joint Providers proposal.[131] As a general matter, the price cap plan applies three factors to a base rate – an Inflation Factor, an Efficiency (or "X") Factor, and Exogenous Costs.[132] The basic formula takes a base rate and multiplies it a factor that reflects an increase due to inflation, offset by a decrease due to efficiencies. The Inflation Factor will be the Gross Domestic Product – Price Index (GDP-PI)).[133] The Efficiency Factor will be set as a figure

[122] Hamilton Comments at 4-5; Hamilton Reply Comments at 7. Hamilton also views the 2005-2006 Fund year differential as an aberration. Hamilton Comments at 5.

[123] *See* Verizon Comments at 1.

[124] AT&T Reply Comments at 3.

[125] The *2007 NECA Filing* indicates a widening gap between the costs of service for traditional TRS and IP Relay. For 2007-2008, the providers' projected costs and minutes of use for traditional TRS, after disallowances, result in a per-minute rate of $1.69. For IP Relay, the same calculation results in a rate of $1.16. *2007 NECA Filing* at 12, 16. In addition, there may be some inherent cost differentials between the provision of traditional TRS and the provision of IP Relay, *e.g.*, IP Relay providers likely save on interconnection fees.

[126] *See* Joint Provider Comments at 3-13. Joint Providers proposed this methodology for both VRS and IP Relay. As discussed below, we decline to adopt this methodology for VRS.

[127] *See* Joint Provider Comments at 2.

[128] *See id.*

[129] *Id.* at 2-3.

[130] Sprint Comments at 6.

[131] *See* Joint Provider Comments at 3-13.

[132] *Id.* at 6-11.

[133] *Id.* at 6-7.

equal to the Inflation Factor, less 0.5 percent (or 0.005) to account for productivity gains.[134] As a result the rate for a particular year will equal the rate for the previous year, reduced by 0.5 percent (*i.e.*, $\text{Rate}_{\text{Year } Y} = \text{Rate}_{\text{Year } Y\text{-}1} (1 - 0.005)$).[135] Reducing the rate by this amount will encourage IP Relay providers to become more efficient in providing the service.[136]

44. We will also adjust the rate, as necessary, due to exogenous costs, *i.e.*, those costs beyond the control of the IP Relay providers that are not reflected in the inflation adjustment.[137] Therefore, to the extend the Commission adopts new service requirements, we will determine whether the costs of meeting the new requirements warrant an upward exogenous adjustment.

45. In addition, we believe that the three-year rate period for IP Relay, as set forth in the Joint Providers Comments, is a reasonable approach.[138] The first rate period will be the 2007-2008 Fund year, and the rates will continue, with the annual adjustment for productivity gains, through the 2009-2010 Fund Year. After that time, we will reassess what the base rate should be for the next three year period. We note that commenters assert that a multi-year rate provides consistency that is necessary for planning and budgeting purposes, and avoids having to possibly adjust on short notice to a lower rate.[139] We conclude that the IP Relay rates should be adopted for a three-year period.[140]

46. Finally, we do not believe it is necessary to adopt tiered rates for IP Relay, as we do below for VRS. First, there is not the same size disparity among IP Relay providers as there is with the VRS providers. Second, the IP Relay rates have been much lower than the VRS rates, and have not varied significantly over time. Therefore, we believe that a single IP Relay rate, subject to price caps, is appropriate for IP Relay.[141]

3. The Cost Recovery Methodology for VRS

47. We conclude that we will continue to base the VRS rate on the providers' projected costs and minutes of use, and other data submitted to the Fund administrator by the providers, subject to appropriate review and, where necessary, disallowances. However, we will no longer apply a single weighted average rate to all providers. Instead, we will adopt tiered rates based on the monthly minutes

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[134] *Id.* at 7-10.

[135] *Id.* at 10.

[136] *Id.* at 7.

[137] *Id.* at 10-11.

[138] *Id.* at 4.

[139] *See id.* at 4; Sprint Comments at 4.

[140] We do not believe it is necessary to amend our rules in this regard. The current regulations provide that the "payment formulas and revenue requirements shall be filed with the Commission on May 1 of each year, to be effective the following July 1." 47 C.F.R. § 64.604(c)(5)(iii)(H). The Fund administrator's annual May 1st filing must still address all the "payment formulas" (*i.e.*, cost recovery methodologies) mandated by the Commission, the resulting rates that they have calculated for each form of TRS under those methodologies that will be effective in the upcoming Fund year, and the Fund size and carrier contribution factor that results from those rates and the Fund administrator's projected demand for each service.

[141] Providers of IP Relay will still be required to file annual cost and demand data with the Fund administrator, as they have in the past. We believe that this information, which includes actual costs for prior years, will be helpful in reviewing the compensation rates resulting from price caps and whether they reasonable correlate with projected costs and prior actual costs. We will also need this information to evaluate the new base rate every three years.

of use provided. These rates will be set for a three-year period, and be reduced annually by 0.05 percent to reflect productivity gains. They may also be subject to other adjustment as provided below.[142]

48. In the *2006 TRS Cost Recovery FNPRM,* the Commission sought comment on whether modifications should be made to the current cost recovery methodology for VRS, or whether there is a methodology other than the current compensation scheme that is more appropriate. The Commission expressed concern, based on comparisons of VRS providers' cost and demand projections with their actual historical data, that some VRS providers have received compensation significantly in excess of their actual costs.[143] The Commission also observed that providers' demand forecasts for VRS generally have been lower than actual demand, resulting in overcompensation to providers for completed minutes under the current per-minute cost recovery scheme.[144]

49. In addition, the provision of TRS under the ADA is intended to give persons with hearing and speech disabilities access to nation's telephone network so that they can call voice telephone users, and *vice versa.*[145] We have also explained that "because Title IV places the obligation on carriers providing voice telephone service to also offer TRS to, in effect, remedy the discriminatory effects of a telephone system inaccessible to persons with disabilities, the costs of providing TRS are really just another cost of doing business generally, *i.e.,* of providing voice telephone service."[146] As a result, the Commission concluded that the "reasonable" costs of providing service for which providers are entitled to compensation do not include profit or a mark-up on expenses.[147] Providers are entitled to their reasonable costs of providing service consistent with the mandatory minimum standards, as well as an 11.25% rate of return on capital investment so that they are not left to finance reasonable capital investments out of pocket.[148]

50. Many commenters support a cost recovery methodology for VRS that is based on price caps, with an initial rate of the present $6.644.[149] The Joint Providers, for example, assert that the initial

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[142] *See generally* Joint Provider Comments at 2-13; Sorenson Comments at 27-40; Hands On Comments at 36-37; Sprint Nextel Comments at 5-7 (supporting price caps for all forms of TRS, including VRS and IP Relay). Aside from Sorenson, Hands On, and Sprint Nextel, the Joint Providers also include CAC, CSD, GoAmerica, and SNAP.

[143] *2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8392, para. 29. This concern is confirmed by a review of the providers' more recently filed actual (or annualized actual) costs and minutes of use contained in their cost data submission for the 2007-2008 Fund year. Because of our confidentiality rules, we address matters relevant to the providers' cost and demand only in the aggregate. *See* 47 C.F.R. § 64.604(c)(5)(iii)(I).

[144] *2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8392, para. 29. The fact that at least some VRS providers have been overcompensated is reflected in the *2007 NECA Filing,* which indicates that in 2006 VRS providers' actual cost of providing service (based on providers actual costs, without any disallowances, and actual minutes billed) was $4.5568 per-minute – almost one-third less than the rate paid of $6.644 per-minute. *2007 NECA Filing* at Ex. 1-4b.

[145] *See, e.g., 2004 TRS Report & Order*, 19 FCC Rcd at 12479-80, para. 3.

[146] *Id.*, 19 FCC Rcd at 12543, para. 179.

[147] *Id.*, 19 FCC Rcd at 12542-45, paras. 177-82. The Commission found that the providers' average mark-up of 27.2% was "inconsistent with the intent of the statutorily mandated TRS cost recovery scheme" and "plainly not cost-based." *Id.*, 19 FCC Rcd at 12545, para. 182.

[148] *Id.*, 19 FCC Rcd at 12544-45, para. 182.

[149] *See generally* Joint Provider Comments at 2-13; Sorenson Comments at 27-40; Hands On Comments at 36-37; Sprint Nextel Comments at 5-7 (supporting price caps for all forms of TRS, including VRS and IP Relay). Aside from Sorenson, Hands On, and Sprint Nextel, the Joint Providers also include CAC, CSD, GoAmerica, and SNAP. *See supra* note 82. Verizon proposes a similar plan that would set a base rate for three years, subject to annual adjustment to account for inflation and exogenous costs. Verizon Comments at 7-8; *see also* Verizon Reply

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rate should be the present rate of $6.644, and that the price cap methodology would include a price indexing formula to account for inflation, productivity gains, and additional costs, as described above.[150] They further assert that the productivity factor (or X-factor) should be established in a manner that takes advantage of incentives to become more efficient and also ensures that cost savings from efficiency gains are shared with contributors to the fund; Sorenson specifically suggests following the price cap indices used for the local exchange companies (LECs).[151] Sorenson asserts that a price cap approach is appropriate because providers do not compete on price, and therefore it would create incentives to innovate and lower costs.[152] Hands On asserts that the use of price caps will provide a simple and stable means to calculate rates.[153]

51. Commenters suggest that price caps should remain in effect for a minimum of three years.[154] Commenters argue that stable pricing will give providers the opportunity to budget their costs more effectively, and provide enough stability to make long-term investments and allocate money to programs that will reduce costs in the future.[155] Joint Providers suggest that the price cap must be adjusted to account for the capital-intensive nature of the telephone industry as opposed to the labor-intensive nature of VRS and IP Relay.[156]

52. We decline to adopt the price cap methodology as proposed. Instead, in order to compensate VRS providers in a manner that best reflects the financial situation of all providers, we will adopt tiered rates for VRS based on the providers' projected costs and minutes of use, and other data submitted to the Fund administrator by the providers, subject to appropriate review and, where necessary, disallowances. The tiers will be based on the monthly minutes of use provided. We believe that doing so may more appropriately reflect the financial situation of all providers. Presently there are eleven VRS

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Comments at 2. AT&T opposes the Joint Providers' proposal, but views Verizon's proposal as "a more reasoned approach." AT&T Reply Comments at 5. As noted below, in subsequent *ex parte* meetings some providers favored a tiered rate approach. In addition, Sprint Nextel, Snap, and Sorenson jointly submitted a proposal they would be willing to support if a tiered rate methodology were adopted. *See* Michael B. Fingerhut *Ex Parte* (June 27, 2007).

[150] *See* paras. 42-43, *supra;* Joint Providers Comments at 11; *see also* Sorenson Comments at 27-29, 38. Verizon suggests that the initial rate should be $7.01. Verizon Comments at 9 n.19.

[151] *See* Joint Providers Comments at 3-5. According to Sorenson, the price cap indices used for the LECs have three main components: "(1) a measure of the previous year's inflation; (2) a measure that reflects the extent to which the annual productivity gains of the telephone industry are expected to exceed the annual productivity gains of the economy as a whole; and (3) a provision for 'exogenous' cost changes- principally changes in costs that are beyond the telephone company's control, such as a cost increase caused by a change in FCC regulations." Sorenson Comments at 30. Hamilton argues, however, that the "X-factor" proposed may not reflect actual cost trends in the industry. Hamilton Reply Comments at 9. Hamilton urges the Commission to further consider the reasonableness of all VRS costs. *Id.* at 11.

[152] Sorenson Comments at 27.

[153] *See, e.g.,* Hands On Comments at 36. Hands On also asserts that, "the primary merit in that methodology is that it encourages providers to limit costs and to improve efficiency while avoiding excessive expenditure of public and private resources in making rate determinations." *Id.* at 36-37.

[154] *See* Sorenson Comments at 27-28; Joint Providers Comments at 2.

[155] *See* Hands On Comments at 36; Sorenson Comments at 27.

[156] *See* Joint Providers Comments at 5-6. Joint Providers also suggest that the Commission should conduct a review every three years addressing: (1) whether the price cap plan is promoting the achievement of statutory goals for each service; (2) whether there has been an increase in the number of VRS minutes provided, the number of interpreters, and the impact of these factors on interpreter training; (3) the net entry or exit of providers; (4) and changes in quality levels. *Id.* at 12-13.

providers, and these providers are not similarly situated with respect to their market share and their costs of providing service.[157] For several years now, one provider has a dominant market share, and thus this individual provider's projected minutes and costs largely determine the rate.[158] The record reflects, however, that providers with a relatively small number of minutes generally have higher per-minute costs.[159]

53. In light of these different per-minute costs, we conclude that we will adopt tiered VRS compensation rates based upon call volume, measured by monthly minutes of use submitted to the Fund administrator for payment. We further conclude that, at least initially, there will be three compensation rate tiers. These tiers are intended to reflect likely cost differentials between small providers (including new entrants); mid-level providers who are established but who do not hold a dominant market share; and large, dominant providers who are in the best position to achieve cost synergies. As a general matter, the three-tiered approach is based on market data reflecting the number of monthly minutes submitted to NECA by the various providers. The data reflects that the newer providers generally provide less than 100,000 minutes per month; that other, more established providers (with the exception of the dominant provider) generally provide monthly minutes ranging in the low hundreds of thousands; and that the dominant provider provides minutes ranging in the millions. We therefore believe that using three tiers is appropriate to ensure both that, in furtherance of promoting competition, the newer providers will cover their costs, and the larger and more established providers are not overcompensated due to economies of scale.

54. By adopting a tiered approach, providers that handle a relatively small amount of minutes and therefore have relatively higher per-minute costs will receive compensation on a monthly basis that likely more accurately correlates to their actual costs. Conversely, providers that handle a larger number of minutes, and therefore have lower per-minute costs, will also receive compensation on a monthly basis that likely more accurately correlates to their actual costs. Furthermore, we conclude that under the tiered approach, all providers would be compensated on a "cascading" basis, such that providers would be compensated at the same rate for the minutes falling within a specific tier. In other words, all providers will be compensated at the highest rate for those minutes falling within the first tier; at the middle rate for those minutes falling within the middle tier, and at the lower rate for all additional minutes.[160]

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[157] *See* www.neca.org (Resources, then TRS, then). Some of these providers were companies that offer voice telephone service and offered TRS, and VRS, since their inception (*e.g.*, Sprint, Hamilton). Others are not traditional telephone companies, but have now been offering VRS service for some time (*e.g.*, Hands On, Sorenson). Finally, there are a number of VRS providers certified under the Commissions 2005 certification rules, some of which are have either only recently begun to offer service or only provide a relatively small number of minutes.

[158] *Cf. 2005 TRS Rate Order*, 20 FCC Rcd at 12246, para. 23 (noting that the proposed VRS rate appeared to be driven by the cost and demand data of one provider).

[159] *See* CSDVRS *Ex Parte* (Apr. 5, 2007) (as "a VRS provider gets larger, it can operate its service more efficiently by taking advantage of operating efficiencies[, which] allows larger VRS providers to have a lower cost per-minute cost than smaller VRS providers").

[160] We note that several VRS providers have filed comments addressing the use of tiered rates for VRS. See CSDVRS *Ex Parte* (April 4, 2007); CSDVRS *Ex Parte* (April 5, 2007) (attaching Proposal for a 3-Year Variable Tiered Rate Methodology); Hands On Comments to NECA's May 1, 2007 TRS rate filing, CG Docket No. 03-123 (May 15, 2007); CSDVRS Comments to NECA's May 1, 2007 TRS rate filing, CG Docket No. 03-123 (May 16, 2007); CSDVRS, Hands On, CAC, and GoAmerica *Ex Parte* (May 16, 2007); Hands On Reply Comments to NECA's May 1, 2007 TRS rate filing, CG Docket No. 03-123 at 5-6; Healinc Reply Comments to NECA's May 1, 2007 TRS rate filing, CG Docket No. 03-123 at 3-4; CSDVRS, Hands On, CAC, and GoAmerica *Ex Parte* (June 12, 2007); George Lyon, Jr. *Ex Parte* on behalf of HOVRS (June 26, 2007); Michael B. Fingerhut *Ex Parte* filed by Ruth Milkman on behalf of Sprint Nextel, Snap, and Sorenson (June 27, 2007) (corrected version); George Lyon, Jr. *Ex Parte* on behalf of HOVRS (July 5, 2007); George Lyon, Jr. *Ex Parte* on behalf of HOVRS (July 11, 2007); KPS

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55. The record reflects support for the adoption of tiered rates. Several providers support the following proposal (for ease of reference, we refer to this proposal as the VRS Tiered Proposal)[161]:

- For the first 50,000 monthly minutes of use, which would generally encompass newer providers offering a relatively small number of minutes, the rate would be based on the providers' projected costs and minutes of use: $6.77.[162]
- For monthly minutes of us between 50,001 and 500,000, which would generally encompass established but non-dominant providers, the rate would be based on the $6.77 rate noted above, less marketing (as reflected in the *2007 NECA Filing*[163]) and certain undisputed cost disallowances[164]: the resulting rate is $6.50.
- For monthly minutes of use above 500,000, which would generally encompass providers with a large number of minutes, the rate would be $6.30.[165]

The VRS Tiered Proposal also provides that each of the rates would be reduced annually by 0.05 percent, and that the providers would have the ability to seek exogenous cost adjustments if new costs were imposed that are beyond the providers' control.[166]

56. We conclude that we will adopt tiered VRS rates based on monthly minutes of use, and that initially there will be three tiers. We also conclude that we will set the tiers, and the rate for each tier, for a three year period. We note that in the *2006 TRS Cost Recovery FNPRM,* the Commission sought comment of whether the VRS rate should be set for a two-year, rather than a one-year, period.[167] As noted above, however, the providers' price cap proposal and related comments propose a three-year rate period for VRS.[168] Commenters assert that a multi-year rate provides consistency that is necessary for planning and budgeting purposes, and avoids having to possibly adjust on short notice to a lower rate.[169] We agree, and therefore conclude that the VRS tiers and rates will be adopted for a three-year period. We also will reduce the rates annually by 0.05 percent, and permit the providers to seek exogenous cost adjustments if new costs are imposed that are beyond the providers' control. The annual downward

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Consulting *Ex Parte* on behalf of CSDVRS (July 19, 2007); David O'Conner *Ex Parte* on behalf of Hamilton (August 10, 2007); Ruth Milkman *Ex Parte* on behalf of Sprint Nextel, Snap, and Sorenson (August 10, 2007); TRS Advisory Council *Ex Parte* Comments (September 6, 2007); Karen Peltz Strauss *Ex Parte* (September 21, 2007); George Lyon, Jr. *Ex Parte* on behalf of HOVRS (September 25, 2007); Ruth Milkman *Ex Parte* on behalf of Sprint Nextel, Snap, and Sorenson (October 2, 2007); George Lyon, Jr. *Ex Parte* on behalf of HOVRS (October 9, 2007); Francis Buono *Ex Parte* on behalf of Sprint Nextel, Snap, and Sorenson (October 15, 2007); Ruth Milkman *Ex Parte* on behalf of Sprint Nextel, Snap, and Sorenson (October 23, 2007).

[161] See Michael B. Fingerhut *Ex Parte* (June 27, 2007).

[162] *See 2007 NECA Filing* at Ex. 1-4b.

[163] *Id.*

[164] *See* Michael B. Fingerhut *Ex Parte* (June 27, 2007).

[165] *Id.*

[166] *Id.*

[167] *2006 TRS Cost Recovery FNPRM*, 21 FCC Rcd at 8392, para. 30.

[168] *See* para. 51, *supra*; *see also See* Michael B. Fingerhut *Ex Parte* (June 27, 2007) (proposing setting rates for three-year period).

[169] *See, e.g.*, Hands On Comments at 37.

adjustment for productivity gains will reduce Fund expenditures and encourage VRS providers to gain efficiencies in providing service.[170]

B. The TRS Compensation Rates for the 2007-2008 Under the New Cost Recovery *Methodologies*

1. Interstate Traditional TRS and Interstate STS

57. The 2007-2008 compensation rate for interstate traditional TRS and interstate STS calculated under the MARS plan is $1.592 per-minute. This rate of $1.592 shall apply to traditional TRS beginning on the first day of the month following the effective date of this *Order*.[171] With respect to STS, however, because we are concerned that outreach efforts directed at the STS community have not been effective, for the 2007-2008 Fund year we will add an additional amount of $1.131 per minute to the MARS-based STS compensation rate. The resulting rate is $2.723. This additional sum paid to each provider must be directed toward outreach efforts directed at the STS community, as set forth below.

58. As discussed above, the MARS rate is based on calendar 2006 intrastate TRS and STS data from 49 states and Puerto Rico; Michigan was excluded because they do not compensate the providers based on a per-minute rate. The rate from each state, and whether it is based on conversation minutes or session minutes, is set forth in Appendix E (rates are listed from lowest to highest). All states compensated traditional TRS and STS at the same rate. To determine the MARS rate, total dollars (calculated by multiplying each state's per-minute rate by either session or conversation minutes, whichever the rate is based on) are divided by the total number of intrastate TRS and STS conversation minutes. That calculation is: $100,738,030 divided by 63,275,205, which equals $1.592.[172]

59. We note that the MARS rate of $1.592 represents an increase of $0.301 (approximately 23 percent) from the 2006-2007 rate ($1.291) for traditional TRS. Although this rate is less than the proposed rates set forth in the *2007 NECA Filing*, which range from $1.687 to $1.735 (including both marketing and outreach),[173] we recognize that there is upward pressure on the traditional TRS rate because of declining demand, and expect that in future years the MARS rate may be higher to reflect higher rates paid under more recently adopted state contracts. In any event, because, as discussed above, the MARS rate is based on competitively bid state rates, we believe that it is reasonable.

60. We also note that the MARS rate of $1.592 (unadjusted for outreach) would represent an increase in the STS rate of $0.183 (approximately 13 percent). We recognized that this rate is less than the proposed rates in the *2007 NECA Filing*, which range from $2.605 to $3.455 (including both marketing and outreach).[174] Because of the relatively small volume of STS calls (less than 20,000 minutes were month), historically there has been a greater range in the providers' projections of the STS

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[170] Providers of VRS and, as noted above, IP Relay, will still be required to file annual cost data with the Fund administrator, as they have in the past. We believe that this information, which includes actual costs for prior years, will be helpful in reviewing the reasonableness of rates adopted for each tier, and whether they reasonable correlate with projected costs and prior actual costs. We will also need this information to evaluate rates every three years.

[171] As noted below, the effective date of this *Order* with respect to the 2007-2008 rates adopted pursuant to the new cost recovery methodologies is 30 days after publication in the Federal Register. *See infra* para. 111.

[172] As noted above, we do not include an allowance for working capital because that factor is built into the state rates. *See supra* note 87.

[173] *See 2007 NECA Filing* at Ex. 1-1b. We note, however, that the MARS rate of $1.592 is close to the rate submitted by NECA that is based on adjusted provider costs, less marketing (but including outreach), a rate of $1.635. *Id.*

[174] *See 2007 NECA Filing* at Ex. 1-3b.